## Defence, development expenditures cut in 97-98

# SBP sees GDP growth at 4pc in new year

**By Mohiuddin Aazim**

KARACHI, Dec 31: The current fiscal year is expected to close with a 4 per cent growth in GDP (gross domestic product) against the target of 6 per cent.

"Barring any untoward developments during the remaining part of the (fiscal) year GDP is expected to grow at 4 per cent," according to a State Bank analysis of the prospects for 1998-99. This analysis forms part of SBP annual report for fiscal 1997-98 released here on Thursday.

**Annual report '97-98 summary: Page 20**

"The nuclear explosion and subsequent sanctions had large-scale effects on the economy. In particular, it adversely affected investors confidence," according to the report in an analysis of the developments during the first five months of 1997-98.

"The external sector came under great pressure," says the report adding that during July-November 1998 workers remittances declined by 39 per cent and foreign investment by about two-thirds compared with the same period last year.

"It is expected that in the second half of 1998-99 the economy will recover substantially from the adverse developments since May 1998." The report says all external payments are expected to be regularized soon, arrears of current payments cleared latest by June 1999 and foreign exchange reserves are projected to the range of $1.4-2.0 billion by the end of fiscal year 1998-99.

The report makes it clear that macroeconomic targets were not changed in the wake of nuclear explosion adding that the rate of inflation during the current fiscal year is likely to remain in single digit.

The report said inflation as measured by CPI (consumer price index) rose by 6.6 per cent during the first five months of the year (July-November 1998) compared with the annual target of 8 per cent.

"Other inflows and payments were also affected," says the report.

"On the basis of the trends so far current account balance for the

**Continued on Page 11**

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**Contined from Page 1**

year is likely to decline from 3.2 per cent of GDP during 1997-98 to 3 per cent of GDP (in 1998-99)," the report adds.

It says money supply went up by 2.3 per cent during 1st July-28th November 1998 compared to a larger expansion of 6 per cent in the same period last year.

The report says although the economy has passed through a period of turbulence in the first six months of the current fiscal year the performance for the year as a whole may turn out to be "quite reasonable."

While reviewing the performance of the economy in the last fiscal year the report said GDP growth rate recovered from a record low of 1.3 per cent in 1996-97 to 5.4 per cent against the target of 5.5-6 per cent.

The report said that in certain areas the performance of the economy "would have been less than satisfactory even if no adverse external shocks had taken place in May 1998. This was particularly so in the budgetary area."

"While expenditures were kept in check and budget deficit was lower than last year, it concealed poor revenue performance and slow progress in effecting structural budgetary reforms," said the report. It said CBR's revenue in fact declined from 12.4 per cent of GDP in 1995-96 to 11.7 per cent in 1996-97 and further to 10.6 per cent in 1997-98. "The situation was saved by the decline in world prices of oil which, instead of being passed on to the consumer in the form of lower retail prices, were utilized to realise higher receipts from petroleum surcharge which offset the poor performance of CBR."

"On the expenditure side, development expenditure were cut down further from 3.4 per cent of GDP in 1996-97 to 3.2 per cent (in 1997-98) while interest payment on debt increased from 6.4 per cent to 6.9 per cent." Defence expenditure also declined from 5.1 per cent of GDP to 4.9 per cent.

It said inflation as measured by CPI fell from 11.8 per cent in 1996-97 to 7.8 per cent well within the target of 9 per cent.

It said gross national savings as percentage of GNP (gross national product) rose to 14.5 per cent against the target of 13.8 per cent in 1997-98 from 11.3 per cent in 1996-97.

The report said Pakistan met all the end-March performance criteria under the ESAF/EFF programme with the IMF and data up to the end of May 1998 indicated that the economy was on track for meeting the performance criteria for June 1998. It did not spell out the criteria.

The report said the outstanding level of external debt rose by $1.9 billion to $29.7 billion at the end of 1997-98. It said debt service payments both on account of long, medium and short term debt, fell from $5.1 billion in 1996-97 to $4.7 billion mainly on account of lower amortization payments.

It said total national debt stood at Rs2518 billion or 91.2 per cent of the GDP at the end of June 1998.

The report said overall fiscal deficit declined from 6.3 per cent of GDP in 1996-97 to 5.4 per cent in 1997-98 missing the target of 5 per cent.

Government expenditures stood at Rs599.6 billion showing a 10.8 per cent increase over the expenditures in 1996-97 but were within the budgeted amount of Rs610 billion. It said the current account of the balance of payments declined from $3.8 billion in 1996-97 to $2.1 billion during 1997-98 adding the improvement was the combined result of lower trade deficit and services accounts and higher workers remittances.

The report reveals that current account deficit (excluding official transfers) was largely financed by net inflows of $1.4 billion of long and short term loans, $0.8 billion of foreign investment and $0.2 billion of official transfers, partly offset by net outflows of $0.6 billion under non-resident foreign currency deposits.

The report recommends that while efforts at containing current expenditure should continue, public revenue should be increased not only to meet the revenue requirements budget but to generate surplus for capital budget as well.

"This requires restructuring of the tax system," the report says adding that provincial governments have to mobilize additional resources and public sector enterprises need to be revamped and made profit-generating.

The report says the policy to involve private sector in the production process needs to be pursued more vigorously. "In the public sector, provision of utilities and infrastructure should be the main activity while all other productive activity should be left to be undertaken by the private sector." The report says the banking reforms should be continued with particular focus on reduction of defaulted loans, increasing the share of private sector in banking industry, introduction of deposit insurance, separation of ownership and management, right-sizing of financial institutions and further strengthening of prudential regulation especially in terms of capital adequacy.

Terming the huge national debt of Rs 2518 billion at the end of fiscal 1997-98 as its servicing as "a major national problem," the report says the size of the debt needs to be contained to manageable limits. It says this can be achieved through various policy measures, including debt retirement through the use of privatization proceeds and sale of government property, and by offering shares of public sector enterprises to holders of debt.

"Similarly, dependence on foreign debt should be reduced."

The report recommends that the reliance on traditional items of exports be reduced and export diversification and expansion of export of agriculture and agro-based products be encouraged.

"Finally...it is important that debt creating sources for financing balance of payments deficit are replaced by direct foreign investment and short-term external liabilities are replaced by medium-term debt instruments. The best policy, however, is to promote self-reliance by increasing national saving and promoting consumption austerity."